Supreme Court, U.S.
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No. 04-786

IN THE

Supreme Court of the United States

UNITED STATES OF AMERICA,

Petitioner,

v.

GLENDALE FEDERAL BANK, FSB,

Respondent.

On Cross-Petition for a Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

BRIEF IN OPPOSITION TO CONDITIONAL CROSS-PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether the trial court clearly erred in making its factual finding, based in part on its observation of witness demeanor, that Glendale witnesses testified without fraudulent intent.

2. Whether the trial court clearly erred in making its factual finding that Glendale's fall from capital compliance was caused by the government's failure to perform the contract.

3. Whether the trial court clearly erred in determining that the government failed to prove an offset to Glendale's reliance damages.

PARTIES AND RULE 29.6 STATEMENT

Glendale relies on the Parties and Rule 29.6 Statement included in its Petition for a Writ of Certiorari, 04-626, at ii.

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INTRODUCTION

The government acknowledges that the questions presented by its conditional cross-petition for certiorari "do[] not appear to be [of] sufficient general importance to warrant this Court's review." US Pet. at 12. This Court's standards for certiorari review, however, are exactly the same for conditional cross-petitions as for petitions. See Sup. Ct. R. 12.5 (conditional cross-petition "shall comply in all respects with . . . Rule 14"); *Id.* 14.1(h) (petition shall "amplify[] the reasons relied on for allowance of the writ. See Rule 10"); *Id.* 10 (setting forth standards for granting certiorari).[1] Accordingly, on the basis of the government's admission alone, the conditional cross-petition should be denied.

The government, however, suggests that if the Court grants Glendale's petition, it should also grant the cross-petition so that the Court will have the opportunity to "consider all issues relevant to the proper calculation of damages." US Pet. at 12. Specifically, the government asks this Court to review three fact-bound determinations made by the trial court and unanimously affirmed by the court of appeals. The notion that a grant of certiorari to a review a specific legal issue should be accompanied by a broad review of unrelated factual issues is inconsistent with this Court's rules and practices. The Court reviews specific legal questions, not entire cases, including findings of fact. See Sup. Ct. R. 10 (a petition "is rarely granted when the asserted error consists of erroneous factual findings").

Moreover, under its "two-court rule," this Court has been emphatic that factual error does not warrant review when the trial court and the court of appeals are in agreement about the

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[1] The Court routinely denies conditional cross-petitions when granting certiorari in the main case. *See, e.g., Illinois Council on Long Term Care, Inc.* v. *Shalala*, 526 U.S. 1067 (1999); *Hoover* v. *Ronwin*, 466 U.S. 558, 565 n.12 (1984).

factual findings. See, *e.g.*, *Graver Tank & Mfg. Co.* v. *Linde Air Prods. Co.*, 336 U.S. 271, 275 (1949) ("[a] court of law, such as this Court is, rather than a court for correction of errors in factfinding, cannot undertake to review concurrent findings of fact by two courts below in the absence of a very obvious and exceptional showing of error"); *United States* v. *Ceccolini*, 435 U.S. 268, 273 (1978) (same).

The two-court rule applies with full force here. The rulings challenged by the government's conditional cross-petition are extraordinarily fact-specific determinations subject only to clear-error review on: the absence of fraudulent intent in testifying witnesses, the causation of losses, and whether the government proved an offset to damages. The trial court made findings on each of these issues that were affirmed by the court of appeals and that are fully supported by the record in this case. Equally to the point, the Court's review of the record and resolution of these factual questions would have no bearing on any party other than the litigants in this proceeding.

In order to refute the government's assertions that the trial court and the court of appeals erred, Glendale sets out in detail the record evidence supporting the lower courts' decisions. We apologize for the length of these demonstrations, which were made necessary because the government's factual assertions are contradicted by the voluminous record from the 14-month trial.

At bottom, the government's real agenda in filing this conditional cross-petition appears to be to muddy the waters surrounding Glendale's petition. Glendale's petition presents important legal questions about the availability of the remedy of restitution for a government breach of contract and demonstrates conflicts with decisions of both this Court and other courts of appeals. The government apparently hopes to avert the Court's attention from these important legal issues and conflicts by convincing the Court by means of its conditional cross-petition that Glendale has already been

"overcompensate[d]." US Pet. at 12. This gambit should be rejected. Glendale's petition should be granted, and the Government's admittedly uncertworthy conditional cross-petition should be denied.

COUNTER-STATEMENT OF THE CASE

Glendale relies on the Statement of the Case from its petition, limiting this discussion to aspects of the case made relevant by the government's conditional cross-petition.

As explained in Glendale's petition, in 1981, Glendale entered into a contract with the United States to assume the massive $735 million of net liabilities of First Federal Savings and Loan Association of Broward County ("Florida") in return for the government's promise to include Glendale's resulting goodwill asset of $735 million in its regulatory capital calculations and to amortize that asset over 40 years. See Glendale Pet. at 4. As this Court ruled, it would have been "madness" for Glendale to acquire Florida without the government's capital promise, "for the very existence of [its] institution[] would have been in jeopardy from the moment their agreement[] [was] signed." *United States* v. *Winstar*, 518 U.S. 839, 910 (1996) (plurality opinion). The government's goodwill promise was therefore "a 'cash substitute' to induce a healthy thrift to assume a failed thrift's obligations." *Id.* at 850.

The government withdrew that "cash substitute" in 1989, after only eight years, forcing Glendale to remove $536 million of remaining goodwill from its regulatory capital. For Glendale, this had grave consequences. The trial court found that because of the breach and corresponding withdrawal of goodwill, "Glendale ultimately failed the risk-based capital requirement, in March 1992, and the core capital requirement, in December 1992." 04-626 Pet. App. at 43a; see *Winstar*, 518 U.S. at 858 ("Glendale . . . fell out of regulatory capital compliance as a result of the new rules").

Attempting to stay in capital compliance, Glendale shrank from $25.6 billion in total assets to a low of $14.4 billion. J.A. at A2002127, *Glendale Fed. Bank, FSB* v. *United States*, No. 03-5136, -5139 (Fed. Cir. filed Feb. 11, 2004) ("03-5136 C.A. App."). Government regulators conceded that Glendale's shrinkage "resulted in the deterioration of the bank's core earnings." *Id.* at A2002368, A1003460-61. Moreover, Glendale was forced to sell its Florida franchise in 1994 and fund the more than $3 billion transfer of Florida's deposits by incurring expensive wholesale borrowings during an upward spike in interest rates. *Id.* at A1007180-81, A1007210, A1003789-90.

After a fourteen-month trial in 1997 and 1998, the trial court awarded Glendale restitution and wounded bank damages. Although the court could not quantify lost profits, it found that Glendale "would have benefited handsomely in the market had the government honored its goodwill promise." 04-626 Pet. App. at 54a, 58a; see also *id.* at 58a n.3 ("[T]he court believes, given the other testimony about the strength of Glendale's management, its strong retail networks in California, Florida, and Washington, and the state of the economy over the last 10 years, that it would have done very well with its foregone assets . . . .").

The largest component of Glendale's wounded bank damages was the $335.4 million it lost when "Glendale lost an historical cost [of funds] advantage over its competitors because the government's breach ultimately forced Glendale our of capital compliance." 04-626 Pet. App. at 74a-75a. As government reports and regulators confirmed, Glendale's *widely-publicized* capital compliance failure caused Glendale to experience billions of dollars in deposit outflows, leaving it no choice except to pay higher interest rates to stem that "run on the bank" and avoid seizure. 03-5136 C.A. App. at A2001986, A2003502 (charts showing deposit outflows and an increased comparative cost of funds after Glendale fell out of capital compliance); *id.* at A2002349 ("OTS was of the

view that Glendale had experienced substantial deposit outflows as a consequence of falling out of capital compliance"); *id.* at A2001533 (OTS) ("In an effort to stop the volatile deposit outflow, [Glendale's] management has priced the deposits at the top of the peer group in most categories. Although the rates are inordinately high, given the significant cash outflow, it is an appropriate strategy"); *id.* at A1003649-64, A10003672-76, A1003689-91, A1020724-26, A1007183-84, A2002297, A2000855, A2001695.

In addition to awarding Glendale reliance damages based on these increased costs, the trial court also concluded that Glendale was entitled to "$11.48 million for increased deposit insurance premiums and $4.675 million in increased OTS assessments" as additional "reliance damages suffered as a result of falling out of capital compliance." 04-626 Pet. App. at 75a. The trial court found that these costs "would not have been incurred had there been no contract and consequently no breach." *Id.*[2] In addition, the trial court concluded that Glendale was entitled to $29.232 million in "other increased post-breach costs," consisting of "the transaction costs from the sale of University Savings ($4.472 million), the transaction costs from the 1993 recapitalization ($24.235 million) and custodial fees paid to the Federal Home Loan Bank ($524,932)." *Id.* The trial court found that "[p]laintiff has shown that all these costs were suffered *as a result of the breach*, and would not have been incurred had the bank not fallen out of capital compliance." *Id.* at 75a-76a (emphasis added). Ample evidence, including testimony by a government regulator, supports these findings. *E.g.*, 03-5136

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[2] The government attempts to soft-peddle this conclusion by stating that "[t]he trial court accepted Glendale's assertion that it 'would not have fallen out of [capital] compliance but for its entry into this contract and the subsequent breach.'" US Pet. at 7 (alteration in original) (quoting 04-626 Pet. App. at 74a). The trial court did more than "accept[] Glendale's assertion" of this fact: it made this factual finding after a fourteen-month trial.

C.A. App. at A1009686-94, A1009699-704, A1009716-31; *id.* at A2002367-68 (Glendale paid "increased deposit insurance premiums" as a result of its "severely deficient capital position"), A1005340-44, A1004850, A2001987, A2002129-32.

After a remand, the Federal Circuit ultimately affirmed the trial court's award of reliance damages. It noted that "[p]roof of reliance damages are factual determinations to be made by the trial court on the basis of the evidence presented by the plaintiff thrifts" and that "[g]iven the complexities of reconstructing the transactions and their consequences, absent a compelling showing of clear error, that should be the end of the matter." 04-626 Pet. App. at 9a. The Federal Circuit concluded that it was "unpersuaded that the trial court's factual findings and conclusions regarding reliance damages . . . are clearly erroneous." See *id.* at 6a. The court also chastised the government for "arguing extreme positions" in *Winstar* cases, resulting in seemingly "endless litigation." *Id.* at 9a.

REASONS FOR DENYING THE CROSS-PETITION

The government's conditional cross-petition asks this Court to review three case-specific factual determinations of the trial court that have already been unanimously affirmed by the court of appeals. And, although it does not cite this Court's two-court rule – whose application would mandate denial of the government's conditional cross-petition – even the government recognizes that none of these questions is worthy of this Court's attention. See US Pet. at 12; see also Sup. Ct. R. 10 ("[a] petition for a writ of certiorari is rarely granted when the asserted error consists of erroneous factual findings"); *Graver Tank & Mfg. Co.*, 336 U.S. at 275 (factual error does not warrant Supreme Court review where the district court and court of appeals are in agreement). In any event, the government utterly fails to show any error in the lower courts' disposition of these questions, much less the

"very obvious and exceptional showing of error" necessary to obtain this Court's review. *Id.*

First, the government claims that the courts below created a "hindsight" "exception" to 28 U.S.C. § 2514, the statute that voids fraudulent claims on the government fisc. It did no such thing. Instead, on clear-error review, the Federal Circuit affirmed the trial court's determination that the Glendale witnesses whose testimony the government attacks had no fraudulent intent. The trial court's factual finding was amply supported by the record.

Second, the government attacks Glendale's causation proof, arguing that the trial court erred in finding that Glendale's reliance on the contract caused it to fall out of capital compliance. Although this entirely fact-bound issue is unworthy of this Court's review, the trial court's causation findings are fully supported by the record.

Third, the government contends that Glendale's reliance damages were not properly "offset" by Glendale's reduction in liabilities – called a "premium" in the banking industry – when it sold its Florida franchise in 1994. But, for an affirmative defense of a reliance damages offset, the *government* would have to prove that Glendale received a *net* benefit from its Florida franchise. This means showing that, over its 13 years of ownership, Glendale received more from Florida's assets than it paid for Florida's liabilities. As the government acknowledged before the trial court, it never even attempted to perform such an analysis. In light of the government's manifest failure of proof, the lower courts' determination that the government did not carry its burden of proving an offset is not error, much less clear error.

I. THE TRIAL COURT'S FACTUAL FINDING THAT GLENDALE WITNESSES' TESTIMONY WAS NOT FRAUDULENT WAS WELL SUPPORTED.

The government claims that the courts below created a "hindsight" exception to 28 U.S.C. § 2514 and then based its rejection of the Government's fraud argument on that exception. Both parts of the government's argument are wrong. The courts below created no such "exception." The trial court simply correctly described certain opinion testimony as necessarily being given in hindsight in its description of why Glendale did not commit fraud. And the Federal Circuit affirmed the trial court's credibility-based finding of no-fraud for the simple reason that the Government fell well short of demonstrating that finding was clearly erroneous. That factbound determination, insulated by a highly deferential standard of review, is not worthy of this Court's attention.

1. The testimony at trial that the government deems fraudulent were not statements regarding a then-existing fact. Rather, they were opinions about what Glendale would have done if the government had not breached its good-will promise. As the *government* correctly emphasized at trial, by definition, Mr. Trafton's and Ms. Snyder's testimony about what they "would have" done in 1990-91 absent the breach in a situation that never existed concerning assets Glendale "would have" held, was "opinion" testimony, not fact testimony about what Glendale actually did. J.A. at A1001293-96, A1020381-82, A1020401-04, A1020715-17, *Glendale Fed. Bank, FSB* v. *United States*, No. 99-5103, -5113 (Fed. Cir. filed Dec. 13, 1999) ("99-5103 C.A. App.").

In a commonsense observation, the trial court noted that "*post hoc* reconstructions of this sort are likely to be colored by knowledge of what actually happened." 04-626 Pet. App. at 56a. Such "color[ing]" does "not rise to the level of a showing of fraud," but instead reflects the common tendency

to "think about what [one] would have done [in the past] with the benefit of hindsight." *Id.* The trial court, which had the opportunity to examine the demeanor of these witnesses, accordingly rejected the government's fraud claim.

The trial court's approach and its ultimate factual finding of no fraudulent intent were entirely consistent with settled law on § 2514. A determination of whether a witness testified with fraudulent intent requires consideration of the witness's entire testimony. *E.g.*, *Ingalls Shipbuilding, Inc.* v. *United States*, 21 Cl. Ct. 117, 126 (1990); *United States* v. *Tonelli*, 577 F.2d 194, 197-98 (3d Cir. 1978). Section 2514 is not violated by a statement that was "negligen[t]" or "incorrect." *Miller* v. *United States*, 550 F.2d 17, 22 (Ct. Cl. 1977). In particular, an inaccurate statement is not fraud when it was based on "confus[ion]," *id.*, or "a misconstruction." *Terrill* v. *United States*, 35 Ct. Cl. 218, 222 (1900); *id.* at 222-23 (no fraud for "[d]iscrepancy" or "exaggerated statements in pleadings or proof," or where explanation left "room to doubt actual fraud"). Moreover, honestly held opinion testimony is not fraudulent. *Soukaras* v. *United States*, 140 F. Supp. 797, 800 (Ct. Cl. 1956). It is *not* fraud to give inconsistent opinions when different factors inform a subsequent analysis made in good faith. *McCarthy* v. *United States*, 670 F.2d 996, 1005-06 (Ct. Cl. 1982).

It is therefore not surprising that the Federal Circuit made short work of the government's fraud claim. At oral argument, government counsel attempted to open with this argument but was immediately told by the Court to move on because it was not "troubled" by the government's argument.[3]

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[3] Mr. Cohen: . . . .With respect to the stories on the fraud aspect –
JUDGE MAYER: Let me suggest to you that we're not deeply troubled by the – we don't need any further recitation of the fraud issue, that's well covered in the briefs, and if you would just get to the arguments on restitution and damages, we would appreciate it.
Transcript of Oral Argument at 2-3, *Glendale Fed. Bank, FSB* v. *United States*, 99-5103 (Fed. Cir. July 7, 2000).

Then in its opinion, the Federal Circuit "briefly dispose[d]" of the Government's fraud arguments in three paragraphs. The court noted that "the question of whether the conflict in the testimonies evidence an intent by Glendale to defraud the Government is a question of fact" and was based on the trial court's "examining and hearing the evidence, and observing Glendale's employees and their demeanor." 04-626 Pet. App. at 28a, 29a. It accordingly reviewed "the trial court's findings under the clearly erroneous standard." *Id.* at 29a. The Federal Circuit went on to quote the trial court's explanation for its factual finding that there was no fraudulent intent on the part of the Glendale witnesses, and then concluded that this factual finding was not clearly erroneous. *Id.* at 29a-30a. This factbound, highly deferential affirmance manifestly did not create a hindsight "exception" to § 2514. Cf. US Pet. at 13.

2. The government mentions – but then abandons – a claim of legal error when it asserts that the Federal Circuit required the government to prove its fraud claim by clear and convincing evidence. *Id.* at 19-20. As the government acknowledges, however, this issue is not material to this case. *Id.* at 20. The trial court did not apply the clear and convincing standard, but nonetheless rejected the government's fraud claim. See 04-626 Pet. App. at 54a-56a. In any event, the government does not offer a question presented on the burden of proof; nor could it do so, in light of its representation to the Court that determination of the appropriate burden of proof is immaterial to the government's claim. US Pet. at 20.

Moreover, the government's proposed analogy between Federal Circuit precedent invoking the clear and convincing evidence standard for *forfeiture* under § 2514 and this Court's decisions applying a preponderance standard under distinct, fraud-based statutory provisions for compensatory damages is flawed. Because fraud under § 2514 voids "the entire claim, including those portions which would have been awarded

absent the fraud," it is a forfeiture provision, rather than one for ordinary damages. US Pet. at 12. The Federal Circuit's use of the clear and convincing standard simply reflects the fact that an outsized penalty such as forfeiture requires a heightened standard of proof before imposition. See *Miller*, 550 F.2d at 22 ("fraud, *resulting in forfeiture*, can be found only on the basis of clear and convincing evidence") (emphasis added); *Chelsea Factors, Inc.* v. *United States*, 181 F. Supp. 685, 691 (Ct. Cl. 1960) (same). The cases cited by the government, US Pet. at 19-20, do not involve forfeiture provisions and are therefore inapposite.

3. In all events, the "inconsistencies" claimed by the government as a basis for requiring a finding of fraud as a matter of law evaporate upon close examination of the voluminous record in this case – a necessary task for review of this issue but one not meriting this Court's attention. This much is clear: Glendale's witnesses admitted that Glendale had both breach and non-breach reasons for exiting higher risk-weighted lending.

(a) As Glendale always admitted, Glendale did not exit higher risk-weighted lending in Southern California until after the breach, in 1990-91. 99-5103 C.A. App. at A1002255-57, A1002274.

(b) Again as Glendale admitted, one reason supporting exiting higher risk-weighted lending in Southern California in 1990-91 was Glendale's breach-induced lack of regulatory capital (the "Breach Reason"). *Id.* at A10006688, A1020626-28, A1020856-57, A1003985-86, A1004014-16, A1004033-34, A1004037-38. As government witnesses conceded, however, there were other reasons for Glendale to exit higher risk-weighted lending in Southern California. These included economic conditions, risk/return assessments, and other provisions of FIRREA that penalized higher risk-weighted lending but did not breach Glendale's contract (collectively, the "Non-Breach Reasons"). *Id.* at

> A1014290-92, A1013094-96, A1013890-98, A1013954-55, A1013967, A1022213-15, A1003343, A1003364-65, A1012788, A2002159-62, A2002164, A4000166-67, A1004006. Indeed, Glendale's contemporaneous Board minutes, strategic plans, disclosure documents, and communications with OTS indicated that Glendale had important Non-Breach Reasons for exiting higher risk-weighted lending in 1990-91. *Id.* at A2000685-86, A2000866-67, A2000917-18, A2000931-33, A2000526-27, A2000529-30, A2000533, A2000566, A2000571-72, A2001661-62, A2001724-25, A2002525, A2002161-62, A2002231, A1004302.

The disputed issue at trial was whether absent the breach, the Non-Breach Reasons by themselves "would have" led Glendale to exit higher risk-weighted lending in Southern California in the same 1990-91 time frame. The government claims that Glendale attempted to defraud the government because Glendale officials who made earlier statements about being "forced" to exit higher-risk lending by the breach later gave opinion testimony at trial that they "would have" made the same exiting decisions for Non-Breach Reasons. Neither set of statements was dishonest.

The earlier statements about being "forced" to exit by the breach were honest, because the breach deprived Glendale of any choice to remain in higher risk-weighted lending. Moreover, Glendale had a reasonable, good-faith basis for believing at the time of these earlier statements that exiting such lending would result in lost income. Mr. Trafton's affidavit correctly noted that Glendale's higher risk-weighted lending "historically [had] been very profitable," *id.* at A3000172, and he testified consistently at trial that at the time of the exiting decisions:

> We had some concern and expectation of return on these business lines that was substantial, and at the time we didn't realize how extensive the credit losses would be. So we at the time felt that we were giving up some

> income stream, not only from these loans, but also from the nonreinvestment of the proceeds of the exit of these business lines.

Id. at A1002177, A1002175. The government repeatedly told the trial court that this particular trial testimony *was truthful*. See *id.* at A1023190-91, A4000169-70.

The earlier statements that the government's breach "forced" Glendale to make decisions in 1990-91, however, simply do not answer the question of what Glendale would have done in response had there been no breach – *viz.*, they do not answer the question whether Glendale would have exited the higher-risk lending for the Non-Breach Reasons *if* it had a choice. Absent a breach, Glendale would have had a choice as to what investment strategy to pursue. The uncontradicted testimony was that the Glendale personnel "didn't ask" themselves, at the time of the earlier statements, "would we have taken these actions in the nonbreach world" based on the Non-Breach Reasons. See *id.* at A1002225-26, A1020849, A1020289-91.

It is telling to contrast the government's claim of fraud in its cross-petition to its contemporaneous reactions to Glendale's prior statements that it was forced to exit higher risk-weighted lending. *In 1993*, the government filed briefs stating that Glendale's prior statements about being "forced" were flawed because they failed to address the Non-Breach Reasons for such exiting. The government stated that Glendale's prior statements failed to address "[w]hat other effects the California real estate market may have had on Glendale that are independent of the effects of the contract." *Id.* at A4000119, A4000127. Similarly, the government stated in 1993 that Glendale's prior statements were "flawed" and "unclear" because they confusingly attributed to the breach decisions that Glendale "made not in response to FIR[R]EA's capital provisions, but in response to other [non-breaching] provisions of FIR[R]EA" that penalized higher risk lending by any savings and loan or bank, regardless of

whether it had goodwill. *Id.* at A4000062-63, A400076-77, A4000118. Moreover, *after* Mr. Trafton and Ms. Snyder testified at trial, the government initially stated in 1997 that it would *not* argue that Glendale's prior statements should "estop Glendale from taking other positions." *Id.* at A1007396. In sum, the government expressly understood that the Glendale witnesses' earlier testimony did not take the Non-Breach Reasons into account; no claim of fraud can be sustained when the witnesses subsequently gave opinion testimony that took into account the very factors the government said needed to be considered in 1993.

At trial, Mr. Trafton and Ms. Snyder engaged in the weighing of the Non-Breach Reasons that had not been considered in the earlier statements, and testified honestly that, after such reconsideration, they believed that, absent the breach, the Non-Breach Reasons would have resulted in decisions by Glendale to exit higher risk-weighted lending in Southern California in 1990-91. See *id.* at A1002240-41, A1020847-53, A1004132. This was a new question, and there were new factors that legitimately influenced their analysis.

Moreover, the trial opinion testimony of Glendale's witnesses properly gave weight to facts that did not exist when the prior statements about being "forced" were made in January 1993. After Glendale recapitalized in September 1993, it eventually achieved in 1995, and subsequently maintained, substantial risk-based regulatory capital cushions above the legal minimum of 8%, reaching ratios of 11-12%. See *id.* at A2002518-20. After 1993, therefore, Glendale eventually had the choice it did not have in 1990-91, because it had the regulatory capital to engage in higher risk-weighted lending. Nevertheless, Glendale decided both (a) *not* to begin new originations of the kinds of higher risk-weighted lending it had exited in 1990-91, and (b) to sell in bulk higher risk-weighted assets that remained in its portfolio. Consideration of these post-1993 decisions helped indicate to Mr. Trafton

and Ms. Snyder that, absent the breach, the Non-Breach Reasons would have been sufficient to support exiting such higher risk-weighted lending in 1990-91. See *id.* at A1020295, A1020185-87, A1000863-66, A1003823-24, A1004092-93. Indeed, *government regulators* concluded that these post-1993 decisions indicated that Mr. Trafton had an "allergy to credit risk." *Id.* at A1013531-36, A2002546.

Ultimately, the government's only response to the ample evidence that Glendale's witnesses were honestly responding to new analyses and factors is to argue that they deliberately changed their story in 1997 because they allegedly realized only at that late date that Glendale's higher-risk weighted lending had suffered losses in the 1990s. US Pet. at 17. Not only does this raise a fact-bound issue, it is utter nonsense. As early as Glendale's December *1990* 10-Q, well *before* any of the prior statements about being "forced" were made, Glendale had *publicly* announced $153 million dollars of such losses. 99-5103 C.A. App. at A1004021-22, A2000647.

II. THE TRIAL COURT'S FACTUAL FINDINGS ON CAUSATION WERE WELL SUPPORTED.

The government next complains that the trial court erred in concluding that Glendale fell from capital compliance because of the breach, citing a purported "gap" in Glendale's evidence related to causation. US Pet. at 21-25. The government even goes so far as to suggest that Glendale was better off thanks to the government's breach. *Id.* at 22-23. As the government acknowledges, however, the Federal Circuit did not expressly "address" this specific argument, *id.* at 24, an omission that implicitly reflects the dim view that court took of the government's claim of clear error and that makes its decision an exceedingly poor vehicle for this Court's review. Additionally, this is another record-intensive, factbound question subject to a highly deferential standard of review. In fact, causation is a "classical" question of fact, *e.g.*, *Brooktree Corp.* v. *Advanced Micro Devices, Inc.*, 977

F.2d 1555, 1578 (Fed. Cir. 1992), that the Federal Circuit correctly reviewed only for clear error.

1. The premise underlying the government's challenge to Glendale's "wounded bank" award – that to recover reliance damage, Glendale bore the burden of proving that it would not have fallen out of capital compliance absent the breach – is false. Expectation damages require a plaintiff to prove what would have occurred if the contract had been made by the parties but never breached. As the government concedes, however, reliance damages should put the plaintiff "'in as good a position as he would have been in had the contract not been made.'" U.S. Pet. at 21 (quoting 04-626 Pet. App. 36a (quoting *Restatement (Second) of Contracts* § 344(b) (1981))). A century of precedent establishes that when a plaintiff seeks reliance damages and proves losses it incurred because it entered the contract, the defendant may prove an affirmative defense for "any loss that *the party in breach can prove with reasonable certainty* the injured party would have suffered [anyway] *had the contract been performed.*" *Restatement (Second) of Contracts* § 349 cmt. a & illus. 1-2 (1981).[4] In other words, "[t]o the extent that defendant argues that [plaintiff's] damages should be offset by losses that [plaintiff] would have sustained had the contract been fully performed, *defendant* bears the burden of proof." *Westfed Holdings, Inc.* v. *United States*, 52 Fed. Cl. 135, 155 (Fed. Cl. 2002) (emphasis added). In a brief below, the government conceded that "the party in breach" bears this burden of proof. 03-5136 C.A. App. at A4000566.

Thus, for reliance damages, Glendale's only causation burden was to show that it would not have fallen out of capital compliance "had the contract not been made." Once

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[4] *Accord, e.g.*, *United States* v. *Behan*, 110 U.S. 338, 343-47 (1884) (government contract case); 3 E. A. Farnsworth, *Farnsworth on Contracts* § 12.16, at 282 (3d ed. 2004); J. Calamari & J. Perillo, *The Law of Contracts*, § 14-9, at 557 (4th ed. 1998).

Glendale satisfied this burden, it was the government's burden to show that Glendale would have fallen out of capital compliance if the government had performed its goodwill promise. As we now demonstrate, the trial court properly found that Glendale proved it would not have fallen out of capital compliance *both* (a) had the contract not been made and (b) had the contract been performed.

2. The trial court found that Glendale fell out of capital compliance and suffered wounded bank damages that Glendale "never would have incurred had the contract never been entered." 04-626 Pet. App. at 64a; *see also id.* at 74a; *id.* at 11a (Glendale's wounded bank damages were "suffered as a result of its reliance on the contract"). In making these factual findings, the trial court noted that Glendale

> provided credible evidence, through its highly qualified and perceptive expert Dr. Paul Horvitz, that [it] would not have fallen out of [capital] compliance but for its entry into this contract and the subsequent breach by the government. Dr. Horvitz possessed the unique blend of a brilliant academic and a practical former regulator with an impressive bibliography dealing with issues relevant to this case.

Id. at 74a. Such "credibility determinations by the trial judge 'can virtually never be clear error.'" *First Interstate Bank of Billings* v. *United States*, 61 F.3d 876, 882 (Fed. Cir. 1995); see also *Whitney Benefits* v. *United States*, 926 F.2d 1169, 1178 (Fed. Cir. 1991) (not clear error "that the Claims Court agreed more often with [plaintiff's] experts than it did with the government's").

The trial court's findings are fully supported by other parts of the record as well. Glendale's evidence included that:

> (a) After the government removed the goodwill from Glendale's regulatory capital, the net effect was that entering the contract reduced Glendale's regulatory capital by $527.5 million. 03-5136 C.A App. at

A2002518. This is more than twice the largest amount ($252 million) by which Glendale ever fell out of regulatory capital compliance after the breach, even counting every penny of real estate losses Glendale suffered in California. See *id.* at A1021094-99, A2002518.[5]

(b) In its 60-year pre-breach history, Glendale was managed with sufficient prudence that its regulatory capital was always comfortably above the required minimums. *Id.* at A1021094-99.

(c) Government regulators consistently gave Glendale favorable examination ratings and praised its management and profitability until after the breach. *Id.* at A2001597, A2001581-82, A2001477, A2001977.

(d) Prior to the breach, Glendale proved very successful in diversifying its assets to respond to economic conditions and in raising additional capital; together, these efforts increased Glendale's tangible capital from a *negative* $480,000,000 in November 1981 (because of the assumption of Florida's net liabilities) to a *positive* $423,000,000 in 1989, a $903,000,000 improvement, *id.* at A2002126, A1006168-72.

(e) Glendale's negative post-breach net income for fiscal years 1990 through 1996, *excluding* goodwill written off when Florida was sold, was approximately $258 million. See *id.* at A2002530-33. This was far less than its pre-breach $903 million increase in capital. Thus, as Professor Horvitz testified, (i) if there had been no contract, and (ii) Glendale had acquired other assets that produced the *same* positive net results as Glendale's

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[5] Indeed, federal regulators understood that one of the purposes of Glendale's goodwill was to provide a capital cushion that would keep the bank in capital compliance during recessions by absorbing real estate losses. 03-5136 C.A. App. at 1006744-48, A2002490-92, A2002172, A1002792, A1002899-2900, A1009665-70.

actual non-Florida assets (even *including* the losses from higher credit-risk loans), then (iii) Glendale's capital would have *increased* and Glendale would have remained in capital compliance. See *id.* at A1021094-99.

3. The government has only one response to the trial court's well-supported finding that Glendale would not have fallen out of capital compliance if it never entered the contract. The government argues that Glendale's failure to prove a cash loss from its Florida division must mean that Glendale did not fall out of regulatory capital compliance because of the contract. U.S. Pet. at 23. This argument fails because it confuses two different issues. Wounded bank damages are predicated upon the trial court's finding that Glendale's reliance on the contract caused a massive reduction in Glendale's *regulatory capital*. Whether Glendale's Florida division suffered a *cash loss* is a different issue. The government errs by ignoring this distinction.

The assets supporting regulatory "capital" often are not cash. *Winstar*, 518 U.S. at 846-48, 854-55. Here, the contract allowed Glendale to "book" $734.7 million in "*market value deficit* or net excess liabilities (negative net worth) as supervisory goodwill, an asset for purposes of meeting *regulatory capital* requirements." 04-626 Pet. App. at 26a (emphases added). This conclusively demonstrates that the regulatory capital calculations are not the same as measurements of cash loss or gain.

Before the contract, Glendale was "well capitalized." *Winstar*, 518 U.S. at 861. By contrast, "[a]t the time of the merger, the market value of the liabilities of Broward exceeded the market value of the assets by $734[.7] million." 04-626 Pet. App. at 42a. "[T]o fill the capital hole," so that the Broward acquisition did not destroy Glendale's regulatory capital, the government promised that Glendale could treat $734.7 million of goodwill as an asset for regulatory capital purposes, to be amortized over 40 years. *Id.* Thus, "had

Glendale not been able to treat supervisory goodwill as regulatory capital, it would have become immediately insolvent, with a *capital deficit* of nearly $500 million." *Id.* Because of the contract, however, at the instant after the merger, Glendale had exactly *the same amount* of regulatory capital ($277 million) as it had before the merger. 03-5136 C.A. App. at A1009838-39. Put another way, the contractual treatment of goodwill left Glendale's regulatory capital in "equipoise at the time of the acquisition – at least on paper." *Landmark Land Co.* v. *FDIC*, 256 F.3d 1365, 1370 (Fed. Cir. 2001).

Pursuant to the contract, Glendale wrote off approximately $199 million in goodwill before the breach in accordance with Generally Accepted Accounting Principles. 03-5136 C.A. App. at A4001724-45, A4001747. The breach caused the removal of the remaining $536 million of goodwill from Glendale's balance sheet. *Id.* As the trial court noted, the "transaction . . . altered Glendale's balance sheet radically at the time of the merger ... and then required another massive restructuring of its balance sheet" after the breach. 04-626 Pet. App. at 64a. The net result was that, after the goodwill was removed by the government, and after offsetting all benefits from Glendale's Florida division, entering the contract caused a $527,530,000 million reduction in Glendale's regulatory capital, regardless of whether Florida caused a cash loss. See 03-5136 C.A. App. at A1008590, A1008606, A1008610-11; A2001953.[6]

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[6] The trial court found that the calculations of Glendale's expert, Mr. Plantiko, properly offset every penny of Florida's net income against Glendale's $735 million reduction in regulatory capital from the removal of goodwill. *See* 04-626 Pet. App. at 76a ("Mr. Brad Plantiko of KPMG Peat Marwick has meticulously, and credibly, documented . . . the gross recovery by Glendale from Florida," including "the 1994 premium it received for the sale of Broward, loan accretion, interest rate declines, and loan sale gains."). *See* 03-5136 C.A. App. at A1008590-91, A1008606-11, A2001951.

As the trial court plainly understood, every dollar of goodwill eliminated moved Glendale exactly one dollar closer to falling out of regulatory capital compliance, even if the loss of goodwill was not by itself a cash loss. Indeed, the government's lead expert *agreed* that "Florida used up capital." 03-5136 C.A. App. at A1011898-90. Ultimately, he admitted that "Glendale fell out of capital compliance because it couldn't use goodwill as capital." *Id.* at A1015992, A1010539, A1010466-67. The lower courts' findings on this causation issue are fully supported by the record.

4. Once Glendale established that it would not have fallen out of capital compliance if it did not enter the contract, this shifted the burden to the government, in a reliance damages case, *supra* at 16, of proving that Glendale would have fallen out of capital compliance if the government had fully performed. The trial court properly found that the government did not meet this burden. 04-626 Pet. App. at 62a-63a (finding that there had been no "showing that . . . Glendale benefited from the breach"); *id.* at 58a & n.3 (Glendale "would have done very well with its foregone assets"). Indeed, the government *conceded* in closing argument that what would have occurred absent the breach was too "speculative" for it to prove. 03-5136 C.A. App. at A1023192.

5. In any event, the trial court repeatedly found that "Glendale would *not* have fallen out of [capital] compliance but for [the] breach." 04-626 Pet. App. at 74a (emphasis added); *see also id.* at 20a (Glendale's wounded bank damages are "actual, ascertainable damages suffered by plaintiff as a result of the breach"). The Federal Circuit subsequently held that the trial court's findings that Glendale "would not have incurred [these costs] but for the contract and its subsequent breach" were not clearly erroneous. *Id.* at 5a-6a.

Indeed, although the trial court observed that it could not quantify the amount of Glendale's lost profits caused by the

breach with sufficient specificity, "there were indeed significant lost profits." 04-626 Pet. App. at 54a. Specifically,

> [t]he type of damages inflicted by the breach, the high quality of Glendale's management team, the institution's survival of the breach, and the post-breach world, while many other savings and loans failed, and the current profitability of the institution at the time of trial, all support a strong inference of *substantial profits* in a non-breach scenario.

Id. (emphasis added).

The government asks this Court to reverse these findings as clearly erroneous – because it contends that "Glendale would have pursued in the absence of the breach" a losing "high risk investment strategy" until it exhausted all of its regulatory capital, including the $536 million of contractual goodwill. U.S. Pet. at 23. The trial court properly rejected this hypothesis after weighing all the evidence from a 14-month trial. The government offers no reason why this Court should exercise its certiorari jurisdiction to retry the facts of this case. In any event, the government's hypothesis is contradicted by substantial evidence, including:

> (a) *Before* the breach, Glendale exited higher credit-risk lending in Florida and Northern California for economic reasons that the government's lead expert conceded "had nothing to do with FIRREA or the breach." 03-5136 C.A. App. at A1013809-11, A1013919-22, A1013925-32.
>
> (b) Also, as noted above, government regulators and experts conceded that Glendale's reasons for exiting Southern California higher credit-risk lending in 1990-91, after the breach, included economic conditions, risk/return assessments, and other provisions of FIRREA that penalized such lending but did not breach Glendale's contract. Indeed, Glendale Board minutes,

strategic plans, disclosure documents, and communications with OTS indicated that Glendale relied on important non-breach reasons, in addition to the breach, in exiting higher credit-risk lending in 1990-91. See *supra* at 11-12.

(c) Again, as noted above, after Glendale recapitalized in September 1993 and sold Florida and University (another subsidiary) in 1994 and 1995, it eventually achieved risk-based regulatory capital ratios of 11-12%, substantially above the legal minimum of 8%. Nevertheless, Glendale decided both (i) *not* to reenter the kinds of higher credit-risk lending it had exited in 1990-91, and (ii) to sell in bulk the higher credit-risk assets that remained in its portfolio. Government regulators concluded that these decisions indicated that Glendale's CEO, Mr. Trafton, who had joined Glendale in July 1990, had an "allergy to credit risk." See *supra* at 14-15.

(d) Ultimately, even a *government* expert, Nobel Prize winner Morton Miller, testified that Glendale's exiting higher credit-risk lending should *not* "be attributed to the phase-out of goodwill ... [but] to the fact that ... those businesses were losing money *and [Glendale] didn't like to do that*." 03-5136 C.A. App. at A2002542-43. Similarly, the government's own regulators conceded that the breach caused Glendale to *lose* substantial earnings, *id.* at A2002368, A1003460-61; see also *id.* at A1009696-99.

In sum, the trial court had ample basis to find that "Glendale would not have fallen out of [capital] compliance but for . . . the subsequent breach." 04-626 Pet. App. at 74a. Because the trial "court's account of the evidence is plausible in light of the record *viewed in its entirety*," the Federal Circuit properly affirmed. *Anderson* v. *City of Bessemer City, N.C.*, 470 U.S. 564, 573-74 (1985). Specifically, "'[w]here there are two permissible views of the evidence, the fact

finder's choice between them cannot be clearly erroneous. This is so even when the [trial] court's findings do not rest on credibility determinations, but are based instead on physical or documentary evidence or inferences from other facts.'" *Id.* at 574 (citation omitted).[7] Under this Court's two-court rule, there is no basis to review the Federal Circuit's affirmance of the factual findings concerning causation.

III. THE COURTS BELOW PROPERLY FOUND THAT THE GOVERNMENT DID NOT PROVE AN OFFSET.

The government's final argument is that Glendale's wounded bank damages should be reduced because Glendale received a $243 million "benefit" in the form of a premium when the breach forced Glendale to transfer its Florida deposits in 1994. US Pet. at 25-29. This factbound argument is meritless.

1. The government bore the burden of proving any alleged offset to Glendale's wounded bank reliance damages.

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[7] The government attempts to escape the trial court's findings by arguing that the Federal Circuit's 2001 decision found as a matter of law that Glendale would have lost money if the government had not breached. US Pet. at 22. The government cites dictum in that decision's "background" section stating that "'[i]n response to the phase out of goodwill [*i.e.*, the breach], Glendale . . . ceased most high credit-risk lending' and that this aspect of 'shrinking reduced its losses.'" *Id.* (alterations and omissions in original, emphasis omitted) (quoting 04-626 Pet. App. at 27a).

Obviously, the Federal Circuit is the best Court to interpret its own decision. If, as the government contends, the Federal Circuit had already held that Glendale "saved" money as a result of the breach, that Court's first decision hardly would have remanded for a "finely tuned calculation of the *actual losses sustained by the plaintiff as a result of the Government's breach*." 04-626 Pet. App. at 37a. By the same token, its second decision would not have affirmed the trial court's reinstatement of wounded bank damages if the court shared the government's interpretation of its prior decision. This Court does not grant certiorari to reinterpret minutiae in the Federal Circuit's own decisions.

Northern Helex Co. v. *United States*, 634 F.2d 557, 563 (Ct. Cl. 1980). As the government has conceded, reliance damages must put Glendale "'in as good a position as [it] would have been had the contract not been made.'" U.S. Pet. at 23. If the contract had not been made, Glendale would not have had a Florida franchise, with its plusses *and* minuses. To support an offset to reliance damages, therefore, the government had to show that Glendale received a *net* benefit from its Florida franchise. This means showing that, over its 13 years of ownership, Glendale received more from Florida's *assets* than it paid for Florida's *liabilities*.

The government's experts conceded that they had "not done" an analysis of whether Glendale received more from Florida's assets than Glendale paid for Florida's liabilities. 03-5136 C.A. App. at A1015977. All the government's offset theory was based on was that in 1994, Glendale paid Barnett Bank $3.057 billion to induce Barnett to assume Florida deposit liabilities with a face amount of $3.3 billion. *Id.* at A1008601-05, A1003718-21. The "premium" is the $243 million difference. Because Glendale also incurred $22 million in transaction costs, the net "premium" was $221 million. *Id.* at A2001951, A1008610-11. Showing that Glendale *paid* more than $3 billion in 1994 to transfer Florida's *liabilities* (rather than $3.3 billion) does not show a net benefit from all aspects of the Florida division over 13 years. Absent a complete analysis of both Florida's income from assets and expenditures for liabilities, it is no more fair to cherry pick a reduction in Florida's liabilities as proof of a net overall benefit from Glendale's 13-year ownership, than it would be to treat an increase in the value of Florida's assets as proof of a *net* benefit. The government's proposed offset was properly rejected because it failed to even try to address both sides of the ledger.

2. Rather than dispute any of this, the government asserts that it is entitled to an offset because Glendale would not have sold its Florida franchise, and thus would not have received

the "premium *in the absence of the breach*." U.S. Pet. at 27 (emphasis added). This is an argument for an offset against *expectation* damages, see *Northern Helex*, 634 F.2d at 563, not reliance damages, and is thus irrelevant to proving any offset to the reliance damages awarded here.

It is also misleading. Absent the breach, Glendale would have retained Florida deposits that had an improvement in market value of $243 million over their original cost. Even the government's experts agreed that transferring an item for its market value does not create a gain. Trial Tr. at 11156.[8]

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[8] The government mischaracterizes the record when it claims that "the deposits [Glendale] held in its Florida franchise provided a low-cost source of funds." US Pet. at 26. The Florida acquisition did *not* cause Glendale to have a lower cost of funds than other 11th District thrifts. For example, the government's September 1981 examination report documents that Glendale's cost of funds was already substantially lower than its 11th District peer group *before* the November 1981 merger with Florida. *See* 03-5136 C.A. App. at A2001549, A1009696-07. Moreover, shortly after the merger, Florida's deposit rates equaled and eventually became *higher* at times than California's, *id.* at A1014069-71, yet Glendale retained an average 18 basis point advantage over its 11th District peers, *id.* at A2001982-84. Because Florida's cost of funds was increased by the breach, the premium was not paid for any existing cost advantage, but because capital-compliant Barnett could realize subsequent profits from the customer base by reducing the cost of deposits and cross-selling. Trial Tr. at 7316, 8165, 8172-73, 8418-19; *see also id.* at 3542-45. The testimony cited by the government, *see* US Pet. at 26 (citing 03-5136 C.A. App. at A1007180-81), is not to the contrary. In this testimony, the witness said that the transfer of Florida's deposits increased Glendale's cost of funds because it had to be funded quickly by wholesale borrowing *during an interest rate spike*. *See* 03-5136 C.A. App. at A1007180-81.

According to the government's own documents and regulators, Glendale's transfer of Florida's deposits was caused by the breach. *See id.* at A2002490, A2002495 (Office of Thrift Supervision ("OTS") official testifies that even after the 1993 recapitalization, Glendale had to sell Florida in 1994, with the final goodwill phase-out looming on January 1, 1995, "to generate additional capital which OTS felt it was *necessary* for the institution to obtain" (emphasis added)); *id.* at A2005226, A2005228

CONCLUSION

The conditional cross-petition for a writ of certiorari should be denied.

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(OTS June 1994 Examination Report stating "additional capital from outside sources is *required*. [Glendale] ha[s] made significant progress in this area given the proposed *sale of the Florida franchise*. (emphasis added)); *see also id.* at A1004640, A1004681-82, A1005550, A1009331, A1009433-37 (Glendale executive Richard Fink confirming that sale of Florida was necessary to achieve capital compliance and that absent the breach, sale would not have occurred).

For such a quick breach-induced transfer, Glendale had no choice but to replace overnight $3 billion of retail deposits with more expensive wholesale borrowings. In the 10 years before the transfer of Florida in 1994, the retail deposit portion of Glendale's liabilities ranged from 65% to 83%. The breach-caused sale of Florida caused this to fall to 48%. Plaintiff's Trial Ex. 1100Q. And Glendale had to incur wholesale liabilities at the worst possible time – after the 300 basis-point interest rate spike of 1994. Defendant's Trial Ex. 3014. Thus, there would be no basis for an offset even if wounded bank damages had been awarded as expectation damages. This is because, absent the breach, Glendale would have both (a) retained the $243 million improvement in the value of its Florida deposits, and (b) not incurred a higher cost of funds due to a massive wholesale borrowing after a 300-basis point interest rate spike.